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No. 225

In the Supreme Court of the United States

OCTOBER TERM, 1957

C. E. NIEHOFF & CO., PETITIONER

v.

FEDERAL TRADE COMMISSION

ON CROSS-PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE FEDERAL TRADE COMMISSION IN OPPOSITION

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OPINION BELOW

The opinion of the Court of Appeals for the Seventh Circuit (Pet. App. i) is reported at 241 F. 2d 37.

JURISDICTION

The final decree of the Court of Appeals (Pet. App. xii) was entered on March 28, 1957. The cross-petition for a writ of certiorari was filed on June 26, 1957. The jurisdiction of this Court is invoked under 28 U. S. C. 1254 (1).

QUESTIONS PRESENTED

Under Sections 2 (a) and 2 (b) of the Clayton Act, respectively, a seller may defend against a charge of illegal price discrimination by showing (a) that its

price differentials make "only due allowance" for differences in the cost of manufacture, sale, or distribution resulting from the different quantities in which its commodities are sold, or (b) that its lower price was made "in good faith to meet an equally low price of a competitor." The following questions are presented:

1. Whether the Court of Appeals correctly held that there was substantial evidence to sustain the Commission's findings that petitioner had failed to establish that its price differentials were cost-justified under Section 2 (a).

2. Whether price differentials which are part of a nationwide pricing system formulated to meet competition generally, and not designed to meet any specific competitor's lower prices, can be justified as a "good faith" meeting of "an equally low price of a competitor."

STATUTE INVOLVED

Section 2 of the Clayton Act, 38 Stat. 730, as amended by the Robinson-Patman Act, 49 Stat. 1526, 15 U. S. C. 13, provides in part:

> (a) That it shall be unlawful for any person engaged in commerce, in the course of such commerce, either directly or indirectly, to discriminate in price between different purchasers of commodities of like grade and quality, * * * where the effect of such discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce, or to injure, destroy, or prevent competition with any person who either grants or knowingly re-

ceives the benefit of such discrimination, or with customers of either of them: *Provided*, That nothing contained in sections 12, 13, 14–21, and 22–27 of this title shall prevent differentials which make only due allowance for differences in the cost of manufacture, sale, or delivery resulting from the differing methods or quantities in which such commodities are to such purchasers sold or delivered: * * *

(b) Upon proof being made, at any hearing on a complaint under this section, that there has been discrimination in price * * *, the burden of rebutting the prima-facie case thus made by showing justification shall be upon the person charged with a violation of this section, * * *: *Provided, however*, That nothing herein contained shall prevent a seller rebutting the prima-facie case thus made by showing that his lower price * * * to any purchaser or purchasers was made in good faith to meet an equally low price of a competitor, * * *.

STATEMENT

After extensive administrative proceedings, the Federal Trade Commission found that petitioner, a manufacturer and seller of automotive products, had discriminated in price among its customers, in violation of Section 2 (a) of the Robinson-Patman Act, and issued a cease-and-desist order. The Court of Appeals for the Seventh Circuit unanimously upheld the Commission's findings of violation as supported by substantial evidence and affirmed the order, but modified it to postpone its effective date. The validity of such modification is before this Court in *Federal*

Trade Commission v. *Nichoff*, No. 170, this Term, certiorari granted, 353 U. S. 982.

The basic facts are undisputed. Petitioner manufactures, sells, and distributes automotive replacement parts to jobbers on a nationwide basis (R. 1014). It sells at list, and gives all customers a 2% discount for cash payment. Petitioner classifies its customers, on the basis of total annual volume of purchases, into four categories, and grants additional discounts to those in the three top categories. These discounts range from 5% to 16%, and each customer's discount is determined at the beginning of the year on the basis of its purchases during the preceding year (R. 983, 1014–1015). Rebates are given to customers whose actual purchases would have entitled them to a higher discount than they received (R. 984, 995, 1018).

The Commission found[1] that the business of jobbers of automotive parts is "highly competitive" (R. 1017); that such jobbers generally, and some of petitioner's customers in particular, operate on a "very thin margin of profit—4 percent of sales or less" (R. 986); that all jobbers must take the 2% cash discount, since failure to do so in many instances would wipe out or materially reduce profits (*ibid.*; R. 1015–1016); that jobbers must stock "many lines of products * * * consisting of many thousands of individual items" (R. 986); that their profit is made up of an "aggregate of very small amounts on each" (*ibid.*); and that a smaller discount or price differential than that granted by petitioner directly and

[1] With one exception (see *infra*, p. 8), the Commission adopted the examiner's findings (R. 1027–1028).

markedly affects profit margin" (R. 990, 1015). The Commission further found that, as to jobbers located in the same trading area, the record was "clear" that petitioner's customers are in competition with each other and also with jobbers who buy from petitioner's competitors (R. 985, 1015). The Commission concluded (R. 1017) that petitioner's differentials "are substantial and materially influence the competitive position of purchasers who resell respondent's [petitioner's] merchandise in this highly competitive field," and that the "record clearly shows" that petitioner's "discounts and rebates to its favored customers carried a direct potentiality of injuring, destroying and preventing competition among its purchasers" (R. 1016; see R. 991).

Petitioner relied primarily on two defenses before the Commission: that its price discriminations were made in good faith to meet the equally low prices of a competitor (R. 992–993); and that the differentials were justified by differences in the cost of manufacturing, selling, and distributing resulting from the different quantities in which it sells (R. 1003). The Commission rejected both contentions.

With respect to the meeting of competition claim, the Commission summarized the pertinent evidence as follows (R. 1018):

> * * *. The evidence received indicates that the prices of many of respondent's rival independent replacement parts manufacturers are somewhat lower than its prices. The average of respondent's prices is higher than those of its competitors in this category yet lower than

> the prices of original parts manufacturers such as Autolite and Delco-Remy, who likewise sell into the replacement field. Respondent's discount program is generally similar to some but is not identical with the schedules adopted by ten of its principal independent competitors. The respondent has one basic price schedule and it is from this that its various discounts and rebates are granted. Its accounts, as previously noted, are classified for discount purposes at the beginning of each year. The initial decision correctly found that respondent's price differentials are a part of a nationwide pricing system formulated to meet competition generally and not designed to meet exactly any competitor's prices.

Such differentials, the Commission concluded, could not be justified under Section 2 (b) as a "good faith" meeting of "an equally low price of a competitor." In this connection, the Commission pointed out (R. 1019) that, under this Court's decision in *Federal Trade Commission* v. *Staley Mfg. Co.*, 324 U. S. 746, "it is individual competitive situations to which the exemptive provisions of the statute relate and not general systems of competition," and "a pricing program which provides for an inherent pattern of discrimination among competing customers and is geared generally to competing for business and not specifically for meeting competing prices is not within contemplation of this defense."

Petitioner sought to show that its discriminations were cost-justified with respect to three categories

of expenses: (1) costs of processing and filling orders of various dollar amounts; (2) direct sales expenses on a per account basis; and (3) advertising expenses. As to the first category, petitioner presented a time study showing the cost of processing orders of various sizes (R. 1003). From this study, it calculated, for orders of different amounts, the total processing cost per dollar in net billing (*ibid.*). Petitioner then totalled the net annual billings of a customer in any particular discount bracket and divided the result by the number of orders to ascertain the customer's average size order over the year. The latter figure was then multiplied by the total processing cost per dollar of net billing applicable to that size order to obtain the actual processing cost of that customer's business (R. 1004). The Commission concluded, however, that this method involved a "basic fallacy," since petitioner's discounts were not granted on a quantity per order basis, but upon an annual volume basis, and individual customer's orders varied in size. As a result, the total annual volume upon which the discount is given has no relationship to the size of the individual shipments which made up that volume (R. 1004–1006, 1020).

The second category—direct sales expenses—involved primarily salesmen's salaries and travel expenses (R. 1008). Petitioner, by dividing the total expense by the number of accounts served, calculated an annual sales cost per account, and argued that the same sales expenditure therefore produced greater revenue from the larger accounts than from the smaller ones (R. 1009). The Commission held

(R. 1009, 1020–1021), however, that petitioner had failed to establish by "reliable and substantial proof" (R. 1010) the assumption upon which this calculation rested—namely, that the salesmen made the same number of calls per year on each customer regardless of size (R. 1009), and that petitioner's "general and conjectural" evidence on this issue was "refuted by specific testimony and evidence showing details of the sales activities engaged in in a typical sales territory" (R. 1020; see R. 1009–1010, 1021).

Similarly, with respect to the third category, petitioner divided its total advertising expenses by the total number of jobber accounts to obtain a per account cost, and then allocated this in the same manner as its sales expenses (R. 1022). With respect to advertising items other than catalogues, the Commission upheld the examiner's ruling (R. 1006–1007) that, since such advertising is general advertising not geared to any particular customer or product, it cannot properly be allocated on a customer basis but must be measured by petitioner's overall sales volume (R. 1022). The Commission reversed the examiner's finding (R. 1007–1008) that cost justification had been established with respect to catalogue expenses, since the "basic premise" of that ruling—that the catalogues were distributed to and used by all of petitioner's customers equally—"is refuted by the record" (R. 1023). It concluded, after reviewing the evidence on this point (R. 1023–1024), that "an allocation of catalogue costs equally among [petitioner's] 886 direct jobbing accounts represents an inaccurate procedure" (R. 1024).

The Court of Appeals, upon a careful review of the facts (Pet. App. i–vi), unanimously concluded (*id.* vii) that there was substantial evidence to support the findings of the Commission that petitioner had failed to show either that its price discriminations were cost-justified or had been made in good faith to meet equally low prices of its competitors.

ARGUMENT

1. Petitioner challenges the Commission's ruling that it failed to establish that its price differentials were cost-justified (Pet. 2, 8–9). Pointing out that this Court has never "determined the nature and extent of the proof required to make out" the defense of cost justification under Section 2 (a), petitioner urges that this Court "should clarify the general principles of acceptable proof available for the establishment" of that defense (Pet. 9).

The determination whether price discriminations "make only due allowance for differences in the cost of manufacture, sale, or delivery resulting from the different methods or quantities" in which commodities are sold necessarily involves primarily factual questions. The standard of proof for establishing this defense is the same as that for establishing any other factual contention—namely, showing by "reliable, probative, and substantial evidence" (Administrative Procedure Act, Section 7 (c), 5 U. S. C. 1006) that the differentials are in fact justified by differences in cost resulting from the different quantities in which the goods are sold.

In the instant case, petitioner's cost defense was based on average costs, and no attempt was made to produce "concrete and specific evidence of cost variances in dealing with different purchasers." *Reid v. Harper & Brothers*, 235 F. 2d 420, 421–422 (C. A. 2), certiorari denied, 352 U. S. 952. The examiner and the Commission carefully reviewed the evidence, but held that it involved a number of basic fallacies and therefore did not accurately reflect actual cost savings. As the examiner concluded (R. 1041), petitioner "has attempted to establish its defense of cost justification in much the same manner as its defense of meeting competition in good faith—generally, instead of specifically, with generalizations and opinion rather than with detailed records which are solely within its knowledge and ability to keep and maintain and under its control." Although it may be difficult to show cost justification (cf. *Automatic Canteen Co. v. Federal Trade Commission*, 346 U. S. 61, 68–69), cost studies, to be acceptable, nevertheless must reflect "with substantial accuracy" the differences in selling costs to the customers in the different price brackets. *American Can Co. v. Russellville Canning Co.*, 191 F. 2d 38, 59 (C. A. 8).

"[T]he burden of showing a cost justification is on the seller in a § 2 (a) proceeding." *Automatic Canteen* case, *supra*, p. 76; see *Federal Trade Commission v. Morton Salt Co.*, 334 U. S. 37, 44–45. The Commission found, as a factual matter, that petitioner had failed to meet that burden, and the Court of Appeals upheld these findings as supported by substantial evidence. That conclusion, we submit, was correct.

and its validity presents no question warranting further review.

2. The Court of Appeals also correctly held that the Commission properly rejected petitioner's claim that its price discriminations had been made in good faith to meet the equally low prices of competitors. The Commission rejected the defense on the ground that "a pricing program which provides for an inherent pattern of discrimination among competing customers and is geared generally to competing for business and not specifically for meeting competing prices is not within contemplation of this defense" (R. 1019). The Commission thus correctly applied the rule that the meeting competition defense "places emphasis on individual competitive situations, rather than upon a general system of competition" (*Federal Trade Commission* v. *Staley Mfg Co.*, 324 U. S. 746, 753) and that Section 2 (b) does not "permit[s] a seller to use a sales system which constantly results in his getting more money for like goods from some customers than he does from others" (*Federal Trade Commission* v. *Cement Institute*, 333 U. S. 683, 725; see also *Federal Trade Commission* v. *National Lead Co.*, 352 U. S. 419, 431).

In *Staley*, the sellers involved "never attempted to establish their own non-discriminatory price system, and then reduced their price when necessary to meet competition. Instead they have slavishly followed in the first instance a pricing policy which, in their case, resulted in systematic discriminations * * *" (324 U. S. at 754–755). Similarly, in the instant case, petitioner's price differentials are "constructed

for all of its competition rather than any particular competitor" (R. 999), and petitioner "maintains its pricing system as is, under the volume discounts established, and never departs therefrom regardless of specific price cutting" (R. 996). We submit, therefore, that the Commission and the court below, in rejecting petitioner's meeting competition defense, correctly applied the holding of this Court in *Staley* and *Cement*—and recently reaffirmed in *National Lead*—that the Section 2 (b) defense cannot be used to justify a general pricing system.[7]

[7] To this extent, the case is similar to *Federal Trade Commission* v. *Standard Oil Company*, No. 24, this Term, certiorari granted, 352 U. S. 950. In that case, to which petitioner makes no reference, the Government is challenging an earlier decision of the court below (233 F. 2d 649) upholding a Section 2 (b) defense where a discount was regularly granted to certain so-called "jobber" customers pursuant to Standard's long-established and inherently discriminatory pricing policy. There, however, Standard argued—and the Commission found—that Standard's pricing policy was also used by some of Standard's major competitors; that Standard and its competitors employed the same criteria for classifying customers as "jobbers"; and that Standard and its competitors granted the discriminatory "tank-car" price to all customers so classified.

In the instant case, petitioner's discriminatory prices did not meet any or all competitive prices in the great majority of instances (R. 999). As the Commission stated (R. 1018): "* * * the prices of many of respondent's rival independent replacement parts manufacturers are somewhat lower than its prices. The average of respondent's prices is higher than those of its competitors in this category yet lower than the prices of original parts manufacturers such as Autolite and Delco-Remy, who likewise sell into the replacement

Petitioner contends (Pet. 7–8) that the decision below conflicts with *Balian Ice Cream Co.* v. *Arden Farms Co.*, 231 F. 2d 356 (C. A. 9), certiorari denied, 350 U. S. 991. There, according to petitioner (Pet. 7–8) the Ninth Circuit "held that a general lowering of prices in good faith to meet the competition of lower prices of various competitors was a complete defense under Section 2 (b) to an alleged violation of 2 (a)." In *Balian*, however, the court held only that there was substantial evidence to support the finding of the trial court that a "blanket price cut" made in the Los Angeles area by a seller of ice cream had been made "in good faith to meet the low prices of some of its competitors" (p. 366). In the instant case, on the other hand, the Commission found that petitioner never had reduced its prices to meet lower prices of competitors, but on the contrary "maintains its pricing system as is, under the volume discounts established, and never departs therefrom regardless of specific price cutting" (R. 996).

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field. Respondent's discount program is generally similar to some but is not identical with the schedules adopted by ten of its principal independent competitors."

In these circumstances, wholly apart from the question of "good faith," it could not possibly be said that petitioner's price discriminations were made "to meet an equally low price of a competitor." It follows that, even assuming *arguendo* that the Section 2 (b) defense in *Standard* were upheld by this Court, the Section 2 (b) defense in the instant case was properly rejected.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the cross-petition for a writ of certiorari should be denied.

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